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Bill Fraher, CPA

TOWN OF ASHBURNHAM

MANAGEMENT LETTER

June 30, 2016



The Board of Selectmen
Town of Ashburnham, Massachusetts

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Dear Board Members:

In planning and performing my audit of the financial statements of the Town of Ashburnham for the year ended June 30, 2016, I considered its internal control structure in order to determine my auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control structure. However, during my audit, I noted certain matters involving the internal control structure and other operational matters that I am presenting for your consideration.

My consideration of the internal control structure was for the limited purpose described in the preceding paragraph and would not necessarily disclose all matters that would be considered reportable conditions under standards established by the American Institute of Certified Public Accountants. In addition, because of inherent limitations in any internal control structure, errors or irregularities may occur and not be detected by such control structure.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A *material weakness* is a deficiency or combination of deficiencies in internal control such that there is a reasonable possibility that a material misstatement of the Town of Ashburnham, Massachusetts' financial statements will not be prevented or detected and corrected on a timely basis. I did not identify any deficiencies in internal control over financial reporting that I consider to be material weaknesses.

Other matters involving the internal control structure and other operational matters are presented in the following report. These matters were considered in determining the nature, timing and extent of the audit tests applied in my audit of the financial statements, and this report does not affect my report on those financial statements dated March 15, 2017. I have not considered the internal control structure since the date of my report.

This report is intended solely for the use of the Board of Selectmen and Town Management and is not intended and should not be used by anyone other than these specified parties.

Bill Fraher, CPA
March 15, 2017

TOWN OF ASHBURNHAM, MASSACHUSETTS
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Section I - Overview of Operating Results

[Please note that the discussion of the Town's financial results is based on amounts in the Town's fund financial statements (rather than the entity wide statements), presented in accordance with Generally Accepted Accounting Principles (GAAP).]

For the year ended June 30, 2016, general fund revenues and transfers (budgetary basis) increased from \$15.1 million to \$15.6 million, an increase of 3.3%. Overall, the Town's general fund revenues were over budget by \$86,307 or 0.6% with no significant variances between budget and actual numbers. At the same time, the Town's general fund expenditures were under budget by \$393,380 or 2.5% due to unexpended budget amounts in various departments.

For the fiscal year ended June 30, 2016, the Town showed an increase in its general fund reserves. At June 30, 2016, the Town's general fund unassigned fund balance (excluding stabilization and capital reserve) was \$625,575, up from \$106,541 at June 30, 2015. The Town's general fund free cash at June 30, 2016 (which is a calculation made by the Department of Revenue utilizing undesignated fund balance and other amounts) is \$556,679, up from \$125,961 at June 30, 2015.

For the fiscal year 2016 budget, the Town budgeted to use \$185,341 in free cash and other available funds to fund budget items (down from \$585,535 for fiscal year 2015). This use of available funds was more than fully replenished by excess revenues and unexpended appropriations (net overall budgetary variance for the year was \$648,081).

The Town has worked hard over the past several years to maintain a positive financial position. The Town has approximately \$1,390,000 in combined free cash, capital improvement and stabilization fund balances (up from \$925,000 last year). This represents approximately 9% of the annual operating budget of the Town, up from 6% last year and in the middle of the 5% to 15% normal target range. As it has done in the past, the Town should monitor the trend of tax revenues, local aid and other receipts and ensure that annual operating budgets are kept within available revenue and other funding sources. The Town should also attempt to build up operating reserves in the coming years.

Section II - Control Deficiencies

Under auditing standards, there are three categories of internal control deficiencies and other matters that can be identified during an audit. These three categories are material weaknesses, significant deficiencies and control deficiencies. Any items that are identified as material weaknesses or significant deficiencies require modification of the auditor's report on internal control and compliance (which is presented in the report on the financial statements).

II-A. Material Weaknesses

There were no material weaknesses noted during this year's audit.

II-B. Significant Deficiencies

There were no significant deficiencies noted during this year's audit.

Section II - Control Deficiencies (continued)

II-C-1. GASB 34

In 2005, the Town implemented GASB Statement Number 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments*. The Town still has some GASB 34 compliance issues that should be addressed. These include:

- Completing the remaining requirements for full accrual accounting (recording debt, capital assets, accrued interest and other accrual items).
- Segregating funds by purpose/type and proper account number (these should also conform with the Department of Revenue's UMAS Manual). For example, currently the Town's enterprise funds – which should all have fund numbers in the 60s, have the following fund numbers: Water Fund -Fund 25, Water Tank Project - Fund 268, Sewer Fund - Fund 651 and Light Fund -Fund 62
- Converting revenues to the categories required for entity wide statements.

The Town should work on eliminating these items in the coming year.

TOWN'S RESPONSE:

- The Town Accountant plans to complete the journal entries requested from the Auditor annually starting in Fiscal 17 in order to complete the remaining requirements for full accrual accounting.
- The Town is looking into creating a new chart of accounts. The Town will either do so by contracting with MUNIS to assist in the conversion to a full UMAS based GL system or alternatively, the Town will seek a software change and address conversion to a compliant UMAS GL system at the switch. Any changes that will take place are expected to be implemented on or before July 1, 2017.
- The Town Accountant plans to work with the Auditor to implement a mapping system through our chart of accounts structure to comply with Entity Wide revenue categories.

II-C-2. Statements of Auditing Standards on Fraud & Risk Assessment

The Auditing Standards Board has issued numerous Statements on Auditing Standards (SAS) related to fraud and risk assessment. One such statement, SAS 99 - *Consideration of Fraud in a Financial Statement Audit*, outlines an auditor's responsibility as it relates to the possibility of fraud. One area where most communities are exposed to fraud risk is the area of miscellaneous cash receipts. Due to the nature of Town operations, it is necessary that certain miscellaneous cash receipts be decentralized at various Town departments. Although the dollars involved are often not material to the financial statements, this situation creates an internal control concern.

The Town has already taken certain steps to address this issue. The Town should monitor this area for possible additional internal control improvements. One possible enhancement is to have periodic internal audits of selected departmental cash receipts, where departmental turnovers are matched to underlying documentation. While other steps could be implemented, the cost of a more tightly controlled system for miscellaneous departmental receipts must be weighed against the related internal control benefits.

Section II - Control Deficiencies (continued)

II-C-2. Statements of Auditing Standards on Fraud & Risk Assessment (continued)

The Auditing Standards Board also recently issued several new SAS that are collectively called the "Risk Assessment Standards". These standards change and expand an auditor's responsibility in reviewing, identifying and assessing risks faced during a financial statement audit. These standards also affect management's responsibilities in this area.

One of the elements of an organization's internal control is risk assessment. Therefore, it is important that the Town periodically perform a risk assessment process to analyze, identify and evaluate areas where the Town may be exposed to various financial risks. As part of this process, the Town should review its systems, procedures and internal controls in all material financial and operational areas to determine if any modifications are required to minimize such risk. The Town should also ensure that it has an ongoing monitoring program in place to periodically test the effectiveness of any related policies and procedures that are in place.

TOWN'S RESPONSE:

- The Town is seeking funding for a Risk Assessment and a Risk Assessment policy through the State's Community Compact Cabinet grant program. If successful, the risk assessment will be conducted and the policy will be activated no later than July 1, 2017.
- The Town is currently conducting departmental assessments in regards to receipt processes and management as well as implementing random Audits.

II-C-3. Light Plant Accounts

In most communities, the Light Plant is allowed separate accounts for depreciation, customer meter deposits and certain other special funds, so that interest earned will stay with the applicable fund. However, Light Plant operating funds are usually commingled with general Town funds (as they are, by law, with other Town funds such as capital projects and most special revenue funds). In Ashburnham, Light Plant operating cash is maintained in a separate account controlled by the Light Plant. The Light Department can authorize transfers from this account and determines when cash is turned over to "regular" Town accounts. In addition, there is a Light stabilization fund not recorded and tracked on the Treasurer's records.

Massachusetts General Law Chapter 41 Section 35 states that the Treasurer shall "receive and take charge of all money belonging to the Town, and pay over an account for the same" and "no other person shall pay any bill of any department". With this in mind, the Town should examine the possibility of commingling operating funds with Town funds, or at least have full control over the operating cash account. In addition, the Light Department should not be allowed to authorize transfers from this account. The Town should also place the Light stabilization account on the Town Treasurer and Accountant's records. Monthly reconciliations of Town general ledger cash to light ledger cash (which have been performed for many years) should continue as an important component of this process.

TOWN'S RESPONSE:

- The Town is in the process of researching how other Communities in Massachusetts with Light Plants handle the "commingling of funds," and hopes to work closely with the Light Plant to rectify the concern.

Section II - Control Deficiencies (continued)

II-C-4 Trust Funds

The Town needs to examine its categorization of trust funds. It is unclear if all funds categorized by the Town are indeed trusts and, if they are, what amounts should be categorized as expendable vs. nonexpendable components.

The Town should research these funds to determine proper categorization and the correct expendable vs. nonexpendable amounts.

TOWN'S RESPONSE:

- Together with the Treasurer the Town Accountant will be reviewing current trust documents to verify and categorize appropriately the funds we currently have in trust funds. We currently categorize our trusts as expendable vs non-expendable and will be verifying that those breakdowns correspond to the original trust documents.

II-C-5. Internal Control Policies and Procedures Manual

The Town does not have a comprehensive internal control policies and procedures manual relating to the accounting and financial operations of all Town departments. This manual can provide many benefits, including the documentation of procedures for ongoing monitoring purposes, the ability to more easily train new staff in policies and procedures that have been approved by management and the setting of consistent practices for all Town departments.

A comprehensive internal control policies and procedures manual should be developed and approved by the appropriate board or committee. This document should be in sufficient detail to establish clear requirements for day to day operations and allow new staff to understand the Town's internal control systems. The Town has just begun the process of creating a policies and procedures manual; this should be completed in the coming year.

TOWN'S RESPONSE:

- The Town has collected template manuals from other communities and will work on creating and implementing a comprehensive internal control policy and procedure manual for July 1, 2017.

Section III - Informational Matters/New Accounting & Auditing Standards

III-1. GASB 45 - Other Postemployment Benefits (OPEB)

For the 2014 financial statements, the Town implemented GASB Statement Number 45, *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. As required by GASB 45, the Town is recognizing its post-employment benefit liability (primarily retiree health insurance) over a 30-year period. This began in 2014 as the Town adopted this benefit for the first time for that year.

At June 30, 2016, the liability on the Town's financial statements is \$1,948,604. This is based on the first three years of recognizing current costs for this liability and amortizing (over a 30-year period) the current actuarial liability of \$5,830,758.

As the Town continues to recognize current year unfunded costs, amortize the actuarial liability and record amounts at future values, this financial statement liability will continue to grow. If unfunded, this actuarial liability is projected to be \$40 million at the end of the thirty-year amortization period. As this liability grows, the Town should consider addressing a possible long-term funding strategy. The size of the unfunded liability and the existence of a funding plan could have an impact on future bond ratings. The Town established an OPEB trust during 2015 which has a balance of \$46,482 at June 30, 2016 (the electric enterprise fund also has a trust fund that has a balance of \$204,342 at December 31, 2015).

In addition, in fiscal year 2017 the Town will be required to implement GASB Statement #74 – *Financial Reporting for Postemployment Benefits Plans Other than Pension Plans*, and in fiscal 2018 the Town will be required to implement GASB Statement #75 – *Accounting and Financial Reporting for Postemployment Benefits Plans Other than Pensions*. While GASB 74 should have minimal impact on the Town's financial statements, GASB 75 will have a significant impact on the Town's financial statements. GASB 75 applies the new GASB 68 pension model to OPEB, requiring that the Town record the full amount of the remaining OPEB liability (that is currently being amortized onto the balance sheet over 30 years) and record various deferred inflows and outflows related to OPEB on an annual basis. The Town should work with the Town's actuary to ensure that information is available to meet compliance with these new GASB statements.

TOWN'S RESPONSE:

- The Town of Ashburnham currently has contracted KMS actuaries to perform the mandated actuarial studies. The Treasurer will provide information regarding employees and benefits upon request for necessary evaluations to take place. The Town Accountant will maintain the financial records regarding the actual expenses related to Postemployment Benefits as well as reconcile the balance in the OPEB trust fund.

III-2. New GASB Statements - GASB 67 and 68: Pensions

Under the requirements of GASB 67 and 68, the regional retirement system's actuarial study (on which pension information required in the Town's financial statements is based) must be within 30 months and one day from the fiscal year end of the audit period. Since the Town's financial statements include the Light Department presented at their prior year end of December 31st, the Light Department audit for 12/31/16 (to be included in the Town's 6/30/17 audit) will only have the Worcester Regional Retirement

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Section III - Informational Matters/New Accounting & Auditing Standards (continued)

III-2. New GASB Statements - GASB 67 and 68: Pensions (continued)

System actuarial study as of January 1, 2014 (more than 30 months from their audit yearend). While the new study as of January 1, 2016, will be available in time for the Town's information required for the 6/30/17 audit, this will not be available in time for the Light's December 31, 2016 audit. This will likely result in a qualified opinion in the Light Department's financial statements which will impact the Town's audit opinion for the 2017 audit.

Accounting firms are working with GASB to final a better solution to this issue, but at this time there are no alternatives to a qualified opinion. Most Towns with December 31st components in their financial statements will have to deal with this same issue for their 2017 audits.

TOWN'S RESPONSE:

- The Town understands that this is an audit issue that is in control of the Regional Retirement System and is applicable to most Towns with Light Departments. We will await further instruction from our auditor when additional information becomes available.